

Office of Chief Counsel  
Internal Revenue Service  
**Memorandum**

Number: **200748001**

Release Date: 11/30/2007

CC:PA;Br6:JCSchwartz

GL-116854-07

UILC: 6103.04-00, 6103.08-04

date: August 17, 2007

to:

(Small Business/Self-Employed)

CC:SBSE

from: Richard Goldman

Branch Chief

(Procedure & Administration)

CC:PA:Br6

---

subject: Disclosure in State Tax Proceeding

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

**LEGEND**

Taxpayer A and B --

State G --

State G Tax Agency --

State G Tax Agency Component --

**ISSUES**

1. Whether a state may redisclose to the IRS the tax information it received from the IRS under IRC § 6103(d) in order for the IRS to assist the state in making disclosure determinations in a state tax administration proceeding.

2. Whether a state may redisclose in a state tax administration proceeding tax information it received from the IRS under IRC § 6103(d).

### CONCLUSIONS

1. Yes, a state may share with the IRS tax information the IRS has disclosed to the state under IRC § 6103(d). In fact, when entering into information sharing agreements with the IRS, states agree to consult with the IRS prior to disclosing tax information in a state tax administration proceeding.

2. State tax officials (State) are authorized under IRC § 6103(h)(4) to disclose returns and return information in a state tax proceeding. Only that tax information that meets the requirements of IRC § 6103(h)(4)(A), (B) or (C) may be disclosed. Pursuant to information sharing agreements entered into between the State and the IRS, the IRS must be consulted prior to disclosure of tax information in a state tax administration proceeding so the IRS can determine whether disclosing the tax information will seriously impair a civil or criminal tax investigation and advise the State to object to such disclosure under IRC § 6103 if impairment is a possibility.

### FACTS

Petitioners A and B are involved in a state judicial tax proceeding before the State G Tax Commission. In the state tax proceeding Petitioners served Interrogatories and Requests for Production of Documents on Respondent, the State G Tax Agency Component. Respondent failed to produce all records requested by Petitioner, claiming that any such disclosure would violate IRC § 6103(d), the provision under which the Respondent received the information from the IRS. Petitioners have filed a Motion to Compel production of the documents and Respondent has asked the IRS assist in responding to the Motion to Compel.

According to the Motion to Compel, the Petitioners allege that the Respondent has relied on documents and information received from the IRS in making its determination that Petitioners underpaid state income taxes. Also according to the Motion to Compel, the Respondent has refused to produce certain of the documents and information received from the IRS.

State G Tax Agency, like those of all other states, has an Agreement on the Coordination of Tax Administration with the IRS for the sharing of return information under IRC § 6103(d). Under the terms of this agreement, the Respondent on December 14 and December 15, 2005 requested the return information of specifically identified individuals. The IRS responded by providing information and authorizing specified IRS employees to discuss the cases of the taxpayers requested by the Respondent. This office has not seen the information provided to Respondent nor have we seen an accounting of the information provided to Respondent. We have been told by Respondent that the information provided by the IRS was responsive to the requests

made under IRC § 6103(d). This office also has not seen a copy of the Interrogatories and Requests for Production of Documents underlying this Motion to Compel. Based on information received from your office we understand that information provided by IRS to Respondent is responsive to the discovery requests.

According to your June 19, 2007 memorandum to this office, while the State G Attorney General's Office has requested IRS assistance in responding to the Motion to Compel, it has been reluctant to supply the responsive information to your office as it is concerned doing so would violate IRC § 6103. Thus, you have received a request to provide assistance but lack the information to do so.

### LAW AND ANALYSIS

IRC § 6103(d) provides:

**(1) In general.** Returns and return information with respect to taxes imposed by chapters 1, 2, 6, 11, 12, 21, 23, 24, 31, 32, 44, 51 and 52 and subchapter D of chapter 36 shall be open to inspection by, or disclosure to, any State agency, body or commission, or its legal representative, which is charged under the laws of such State with responsibility for the administration of State tax laws for the purpose of, and only to the extent necessary in, the administration of such laws,... Such inspection shall be permitted, or such disclosure made, only upon written request by the head of such agency, body or commission, and only to the representatives of such agency, body or commission designated in such written request as the individuals who are to inspect or to receive the returns or return information on behalf of such agency body or commission... However, such return information shall not be disclosed to the extent that the Secretary determines that such disclosure would identify a confidential informant or seriously impair any civil or criminal tax investigation.

Each State, including State G, has entered into two agreements with the IRS, referred to generally as the Basic and Implementing Agreements, to put into place information sharing programs between the State and the IRS in accordance with IRC § 6103(d). While these agreements serve to establish routine bulk sharing of certain agreed upon information between the State and the IRS, the agreements also establish a procedure for the State to request information on an individual basis where appropriate. Based on what we have received from your office it appears as though information requested under such individualized IRC § 6103(d) requests is what is at issue here.

IRC § 6103(h)(4) provides:

**(4) Disclosure in judicial and administrative tax proceedings.** A return or return information may be disclosed in a Federal or State judicial or administrative proceeding pertaining to tax, but only –

- (A) if the taxpayer is a party to the proceeding, or the proceeding arose out of or in connection with, determining the taxpayer's civil or criminal liability, or the collection of such civil liability, in respect of any tax imposed under this title;
- (B) if the treatment of an item reflected on such return is directly related to the resolution of an issue in the proceeding;
- (C) if such return or return information directly relates to a transactional relationship between a person who is a party to the proceeding and the taxpayer which directly affects the resolution of an issue in the proceeding; or

\*\*\*

However, such return or return information shall not be disclosed as provided in subparagraph (A), (B) or (C) if the Secretary determines that such disclosure would identify a confidential informant or seriously impair a civil or criminal tax investigation.

Thus, under the authority, and in accordance with the requirements, of IRC § 6103(h)(4), a State or its representatives can use the tax information received under IRC § 6103(d) in a State judicial or administrative proceeding pertaining to tax. The current proceeding in which the Motion to Compel is pending is such a state judicial proceeding pertaining to tax. Respondent, therefore, is authorized to use and disclose the information it received from the IRS pursuant to its request under IRC § 6103(d) in the proceeding, including in response to discovery requests.

IRM 11.3.32.19 contains procedures that are agreed to by the State and IRS when entering into the Basic and Implementing Agreements for sharing of tax information that must be followed when Federal returns or return information are to be disclosed in a state tax administration proceeding. A State is obligated to notify the IRS in writing of its intention to disclose any such returns or return information in a state judicial proceeding or to any party other than the taxpayer or his/her designee in a state administrative proceeding. IRM 11.3.32.19(4)

The notice, required to be sent at least 30 days prior to disclosure to the disclosure office or manager from which the information was originally received must include certain details about the information to be disclosed including names and other identifying information; tax periods and type of tax involved; a description of the information to be disclosed; the purpose for which the proceeding is to be conducted; and the manner in which the provision of IRC § 6103(h)(4) will apply. IRM 11.3.32.19(5). Thus, not only does IRC § 6103 permit Respondent to share the information with the IRS in making decisions about responding to discovery requests,

but Respondent is obligated to notify, consult and share information with the IRS in making such disclosures.<sup>1</sup>

Prior to the initial disclosure to the State, the IRS should have reviewed the responsive information to ensure it is not covered by a tax treaty or IRC § 6105, wagering tax information under IRC § 4424, Bank Secrecy Act Information governed by the Bank Secrecy Act Re-Dissemination Guidelines, Grand Jury information, or information obtained under immunity procedures as all of this information should not be disclosed to the State. The IRS disclosure official receiving the notice about redisclosure, however, should ensure that none of the information falls within these categories. IRM 11.3.32.19(6) and IRM 11.3.32.17. Additionally, the disclosure official reviewing the information must ensure that if redisclosed in the state tax proceeding, the information would not identify a confidential informant or seriously impair a civil or criminal tax investigation, even if such potential impairment did not exist at the time of the initial disclosure of returns and return information to the State. IRM 11.3.32.19(6) and IRM 11.3.32.17. States will be advised to edit any documents which they intend to disclose in a judicial or administrative tax proceeding in order to delete Federal returns and return information where their disclosure is not permitted by IRC § 6103(h)(4). IRM 11.3.32.19(8). Thus, if the IRS determines that disclosure of the information in the State judicial proceeding will seriously impair a civil or criminal tax investigation, even if the impairment did not exist at the time the information was released to the Respondent, it can direct Respondent to withhold the information under IRC § 6103(h)(4). Likewise the IRS is charged with assisting Respondent to ensure that all provisions of IRC § 6103(h)(4) are met prior to disclosure.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (202) 622-7950 if you have any further questions.

---

<sup>1</sup> Furthermore, this office has previously opined, and it has been memorialized in the IRM, that the IRC section 6103(h)(1) need to know access extends to Federal tax information disclosed to other agencies under Title 26. IRM 11.3.22.4.1(9). Thus, even if the agreements between the State and the IRS regarding the disclosure of information under IRC section 6103(d) and the subsequent use of that information under IRC section 6103(h)(4) did not require notification, consultation and sharing of the information, IRC section 6103(h)(1) authorizes the appropriate IRS employees access to that information when they need to know it for tax administration reasons.